APPENDIX

Revenue Act of 1936, 49 Stat. 1648:

SEC. 14. SURTAX ON UNDISTRIBUTED PROFITS.

(a) *Definitions.*—As used in this title—

* * * * *

(2) The term "undistributed net income" means the adjusted net income minus the sum of the dividends paid credit provided in section 27 and the credit provided in section 26 (c), relating to contracts restricting dividends.

(b) *Imposition of Tax.*—There shall be levied, collected, and paid for each taxable year upon the net income of every corporation a surtax equal to the sum of the following, subject to the application of the specific credit as provided in subsection (c):

7 per centum of the portion of the undistributed net income which is not in excess of 10 per centum of the adjusted net income.

12 per centum of the portion of the undistributed net income which is in excess of 10 per centum and not in excess of 20 per centum of the adjusted net income.

* * * * *

Treasury Regulations 94, promulgated under the Revenue Act of 1936:

ART. 26–2. *Credit in connection with contracts restricting payment of dividends.*—(a) * * * The provisions recognized by the Act are of two general types, as follows:

(1) Those which come within section 26 (c) (1), in that they prohibit or limit the payment of dividends during the taxable year; and

(2) Those which come within section 26 (c) (2), in that they require the payment, or irrevocable setting aside, within the taxable year, of a specified portion of the earnings or profits of the taxable year for the discharge of a debt incurred on or before April 30, 1936.

* * * * *

(c) *Disposition of profits of taxable year.*—Under the provisions of section 26 (c) (2), a corporation is allowed a credit in an amount equal to that portion of the earnings and profits of the taxable year which, by the terms of a written contract executed by the corporation prior to May 1, 1936, and expressly dealing with the disposition of the earnings and profits of the taxable year, it is required within the taxable year to pay in, or irrevocably to set aside for, the discharge of a debt incurred on or before April 30, 1936. The credit is limited to that amount which is actually so paid or irrevocably set aside during the taxable year pursuant to the requirements of such a contract.

Only a contractual provision which expressly deals with the disposition of the earnings and profits of the taxable year shall be recognized as a basis for the credit provided in section 26 (c) (2). A corporation having outstanding bonds is not entitled to a credit under a provision merely requiring it, for example, (1) to retire annually a certain percentage or amount of such bonds, (2) to maintain a sinking fund

sufficient to retire all or a certain percentage of such bonds by maturity, (3) to pay into a sinking fund for the retirement of such bonds a specified amount per thousand feet of timber cut or per ton of coal mined, or (4) to pay into a sinking fund for the retirement of such bonds an amount equal to a certain percentage of gross sales or gross income. Such provisions do not expressly deal with the disposition of earnings and profits of the taxable year. A contractual provision, however, shall not be considered as not expressly dealing with the disposition of earnings and profits of the taxable year merely because it deals with such earnings and profits in terms of "net income," "net earnings," or "net profits."

* * * * *

U. S. GOVERNMENT PRINTING OFFICE: 1941

IN THE

Supreme Court

OF THE

Guy T. [redacted]

PETITION FOR [redacted]
APPLICATION FOR [redacted]
THE UNITED STATES [redacted]
PEALS FOR THE [redacted]

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INDEX.

	Page
Petition for Reconsideration of Denial of Application for Writs of Certiorari to the United States Circuit Court of Appeals for the Eighth Circuit....	1
Previous Opinions	2
Questions Presented	2
Statute Involved	2
Statement	2
Reasons for Granting the Writs	5
Conclusion	5
Appendix	6
Commissioner of Internal Revenue v. The Strong Manufacturing Company	6
Commissioner of Internal Revenue v. Warren Tool Corporation	13
Commissioner of Internal Revenue v. The Ohio Leather Company	14
Commissioner of Internal Revenue v. Michigan Silica Company	14

CASES CITED.

	Page
Antietam Hotel Corporation (123 Fed. (2d) 274)....	3
Commissioner of Internal Revenue v. The Michigan Silica Co., No. 8721 (Reported in 1941 Prentice-Hall Federal Tax Service at paragraph No. 63,092)	3
Commissioner of Internal Revenue v. The Ohio Leather Co., No. 8842 (Reported in 1941 Prentice-Hall Federal Tax Service at paragraph No. 63,091)....	3
Commissioner of Internal Revenue v. The Strong Manufacturing Company, No. 8829 (Reported in 1941 Prentice-Hall Federal Tax Service at paragraph No. 63,075)	3
Commissioner of Internal Revenue v. Warren Tool Corporation, No. 8836 (Reported in 1941 Prentice-Hall Federal Tax Service at paragraph No. 63,090)	3

IN THE

Supreme Court of the United States

OCTOBER TERM 1941

No. 659
No. 660

MOLONEY ELECTRIC COMPANY, *Petitioner,*

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

PETITION FOR RECONSIDERATION OF DENIAL OF APPLICATION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT.

Your petitioner, Moloney Electric Company, prays that this Court reconsider its denial of application for Writs of Certiorari in these cases for the reason that since the denial of such Writs (November 10, 1941) a conflict of decisions has arisen—the Fourth and Eighth Circuits deciding the question in favor of the Government, and the Sixth Circuit in four cases deciding the question in favor of the taxpayers.

PREVIOUS OPINIONS.

This Court denied Certiorari on November 10, 1941. Prior thereto the Eighth Circuit Court of Appeals decided both questions for the Government (R. 106) (120 Fed. (2d) 617), reversing the United States Board of Tax Appeals on the point decided by that Board in favor of your petitioner, and sustaining the Board on the point it had decided adversely to your petitioners.

The Board of Tax Appeals opinion (R. 15) reported in 42 BTA 78 was accompanied by a dissenting opinion (by two Members) sustaining your petitioner on both points (R. 29) (42 BTA 88).

QUESTIONS PRESENTED.

The two questions presented in the application for Writs of Certiorari rest upon whether a contract executed by your petitioner on June 1, 1928 meets the requirements of Section 26(c)(2) of the Revenue Act of 1936.

STATUTE INVOLVED.

Section 26(c)(2) of the Revenue Act of 1936 allows a credit to corporations in the computation of the Surtax on Undistributed Profits, if a contract was executed prior to May 1, 1936 that required the application of earnings to the liquidation of indebtedness.

STATEMENT.

The application for Writs of Certiorari arise in the determination of petitioner's income tax liability for the year 1936.

The contract in question requires payment of:

(1) Two per cent on the largest amount of bonds outstanding during the year; and

(2) Twenty per cent of the earnings in excess of $320,000.

The Board of Tax Appeals held the 2 per cent payment did meet the requirements of the statute as being part of a contract expressly dealing with the disposition of earnings

and profits of the taxable year; but that the 20 per cent of earnings provision did not meet the requirements of the statute as payment was not required until April 1st of the succeeding year. On the 20 per cent point a dissenting opinion held that the payment date did meet the statutory requirement.

The Eighth Circuit held neither provision came within the statute as the 2 per cent was required to be paid in any event and the 20 per cent payment was not required to be made within the taxable year.

At the time the Eighth Circuit decided the instant case no other circuit had construed the statute.

At the time Certiorari was denied no conflict of decision existed.

On the same day Certiorari was denied (November 10, 1941) the Fourth Circuit decided *Antietam Hotel Corporation* (123 Fed. (2d) 274). In this case the question was similar to the 20 per cent question in the instant case and the Court held in accord with the Eighth Circuit.

On December 9, 1941 the Sixth Circuit decided four cases, involving the same 20 per cent point, contrary to the holdings of the Eighth and Fourth Circuits. The cases are:

Commissioner of Internal Revenue v. *The Strong Manufacturing Company*, No. 8829 (Reported in 1941 Prentice-Hall Federal Tax Service at paragraph No. 63,075).

Commissioner of Internal Revenue v. *The Ohio Leather Co.*, No. 8842 (Reported in 1941 Prentice-Hall Federal Tax Service at paragraph No. 63,-091).

Commissioner of Internal Revenue v. *The Michigan Silica Co.*, No. 8721 (Reported in 1941 Prentice-Hall Federal Tax Service at paragraph No. 63,-092).

Commissioner of Internal Revenue v. *Warren Tool Corporation*, No. 8836 (Reported in 1941 Prentice-Hall Federal Tax Service at paragraph No. 63, 090).

All four decisions are set forth in the Appendix.

The Sixth Circuit in its opinion in *Strong Manufacturing Company* (*supra*) distinguishes its decision from that of the Eighth Circuit in the instant case on three grounds:

(1) "There was no showing in that case (Moloney Electric Company) what the earnings of the corporation were".

The record in the instant case shows (R. 28, 55):

"that $240,000 of its earnings for 1936 was used in liquidating its bonded indebtedness."

(2) "when the payment on the indebtedness was made."

The record in the instant case shows (R. 22):

"They were all retired during that year."

(3) "whether the payment was ever made because of any contract requirement;"

The record in the instant case shows (R. 21):

"Section 1. The Company covenants that as a sinking fund for the retirement of debenture bonds issued hereunder it will pay to the Trustee on the first day of June, 1930, and the first day of each succeeding June thereafter, so long as any of the debenture bonds hereby authorized are outstanding, a sum equal to 2 per cent of the largest amount of debenture bonds at any time outstanding, and will also pay on said date to the said Trustee 20 per cent of the net earnings, for the next preceding year, as hereinafter defined, of the Company in excess of Three Hundred Twenty Thousand Dollars ($320,000). The determination of the sum to be paid to the sinking fund from the net earnings shall be made from an audit to be made at the close of each calendar year by a firm of certified public accountants acceptable to the Trustee, and when said net earnings are so determined from said audit, which, in no event, shall be later than the first day of each April, said amount shall forthwith be set aside in a separate fund by the Company and shall be paid to the Trustee as herein provided on the first day of June of each year, beginning in the year 1930."

REASONS FOR GRANTING THE WRITS.

The Eighth Circuit in deciding the instant case gave no consideration to the second sentence of Section 26(c)(2) of the 1936 Revenue Act which provides:

> "For the purposes of this paragraph, a requirement to pay or set aside an amount equal to a percentage of earnings and profits shall be a requirement to pay or set aside such percentage of earnings and profits."

whereas the Sixth Circuit recognized that said sentence was intended to cover situations where, due to a percentage determination, the amount could not be determined until after the last day of the year, stating: (*Strong Manufacturing Company, supra*)

> "Obviously, the result would be to deny such credits to practically all manufacturing and merchandising corporations, and to admit only those financial companies whose earnings and profits are generally susceptible of immediate computation. This would be unjust."

A conflict exists between the Circuits as to the construction and scope of Section 26(c)(2) which should be resolved by this Court, and unless on reconsideration the Writs are granted this petitioner will forever lose its rights.

CONCLUSION.

Wherefore, it is prayed that this Court will reconsider its denial of the application for Writs of Certiorari and on reconsideration grant such Writs to the end that petitioner may have such relief in the premises as to this Court may seem proper.

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January 6, 1942.